

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 98-0458
SALES AND USE TAX
FOR TAX PERIODS: 1995-1996

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Issue

1. Sales and Use Tax- Electronic Pre-Press Equipment

Authority: IC 6-2.5-3-2(a), P.L. 78-1989, IC 6-2.1-2-4, IC 6-2.5-5-3, Gross Income Tax Division v. National Bank and Trust Co., 79 N.E. 2nd 651, (Ind. 1948), Indiana Department of State Revenue v. Cave Stone, Inc., 457 N.E. 2nd 52 (Ind. 1983).

Taxpayer protests the assessment of tax on the electronic pre-press equipment.

Statement of Facts

Taxpayer is a pre-press house. Taxpayer's primary activity is producing composite films and matchprint proofs from transparencies provided by customers. Beginning in 1995, Taxpayer expanded its activities into offset printing, digital photography and poster and sign production. After an audit, Taxpayer protested the assessment of use tax. Taxpayer submitted a brief in lieu of a hearing. Further facts will be provided as necessary.

1. Sales and Use Tax- Electronic Pre-Press Equipment

Discussion

During 1995 and 1996 Taxpayer purchased computer equipment, software, supplies and digital photographic equipment that is used in its pre-press activities. These pre-press activities include scanning, image retouch and manipulation and manual stripping. These processes are all applied to transparencies which customers provide for Taxpayer. Taxpayer protests the assessment of use tax on these purchases.

Pursuant to IC 6-2.5-3-2 (a), Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana. A number of exemptions are available from use tax including those collectively referred to as the manufacturing exemptions. All exemptions must be strictly construed against the party claiming the exemption. Gross Income Tax Division v. National Bank and Trust Co., 79 N.E. 2nd 651, (Ind. 1948).

IC 6-2.5-5-3 provides for the exemption of “manufacturing machinery, tools and equipment which is to be directly used in the direct production, manufacture, fabrication of tangible personal property.”

Taxpayer contends that the protested items qualify for this exemption which requires that qualifying property be directly used in the direct production process. Exemption is only granted to machinery that is used in a production process, the process of manufacturing tangible personal property. Therefore the first issue to be determined is whether the commercial printing process is a process which produces tangible personal property. The 1989 General Assembly enacted a series of amendments in P.L. 78-1989 which dealt with the characterization of commercial printing.

P.L. 78-1989 first amended IC 6-2.1-2-4 to read as follows:

The receipt of gross income from the following is subject to the rate of tax prescribed in Section 3 (a) of this chapter:

...
(7) The business of commercial printing that results in printed materials, excluding the business of photocopying.

From this initial provision in the gross income tax, amendments were then made to other gross income tax, adjusted gross income tax and sales/use tax provisions, cross referencing back to commercial printing as described in IC 6-2.1-2-4. Significantly, P.L. 78-1989 amended IC 6-2.5-5-3 adding the language underscored below that expressly references and incorporates the description of “commercial printing” set forth in IC 6-2.1-2-4.

(a) For purposes of this section:

...
(2) Commercial printing as described in IC 6-2.1-2-4 shall be treated as the production and manufacture of tangible property.

Since the above cited statute defines commercial printing as a manufacturing process, the computers and software will qualify for exemption if they are directly used in this direct production process. In Indiana Department of State Revenue v. Cave Stone, Inc., 457 N.E. 2nd 52 (Ind. 1983) the Court sets forth the test for determining whether a particular item qualifies for the directly used in direct production exemption from use tax. The Court stated that items which are considered essential and integral to the production process meet the requirements of the directly used in direct production language of the statute.

The computers, software, supplies and digital photographic equipment in this situation are essential and integral to the production of Taxpayer’s final product. Therefore they qualify for the directly used in direct production exemption.

Finding

Taxpayer’s protest is sustained.